

No. _____

STATE OF TEXAS,
Plaintiff,

v.

FH1 FINANCIAL SERVICES, INC.
d/b/a FH FINANCIAL SERVICE;
Defendant

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IN THE DISTRICT COURT OF

TRAVIS COUNTY, TEXAS

_____ JUDICIAL DISTRICT

PLAINTIFF'S ORIGINAL PETITION

TO THE HONORABLE JUDGE OF SAID COURT:

Plaintiff, STATE OF TEXAS, acting by and through the Attorney General of Texas, Greg Abbott, complains of FH1 FINANCIAL SERVICES, INC. d/b/a FH FINANCIAL SERVICE, Defendant, or "FH Financial," and for cause of action would respectfully show as follows:

DISCOVERY CONTROL PLAN

1. The discovery in this case is intended to be conducted under Level 2 pursuant to TEX. R. CIV. P. 190.3.

JURISDICTION

2. This action is brought by Attorney General Greg Abbott, through his Consumer Protection and Public Health Division, in the name of the State of Texas and in the public interest under the authority granted him by § 17.47 of the Texas Deceptive Trade Practices-Consumer Protection Act, TEX. BUS. & COM. CODE ANN. § 17.41 *et seq.* (Vernon 2002 & Supp. 2008) ("DTPA") upon the grounds that Defendant has engaged in false, deceptive, and misleading acts and practices in the course of trade and commerce as defined in, and declared unlawful by, §§ 17.46(a) and (b) of the DTPA.

NATURE OF DEFENDANT'S OPERATIONS

3. Defendant operates a for-profit debt settlement company. Debt settlement is a form of consumer debt relief, targeted to consumers with thousands of dollars of unsecured debt.

Consumers interested in debt settlement likely are also considering options such as traditional credit counseling, debt management plans, debt consolidation loans, and possibly bankruptcy.

4. Unlike those alternatives, debt settlement is an aggressive form of debt relief, in which consumers stop paying all of their unsecured debts, and save the money they would normally use to pay those debts. After several months, when the accounts are in default, the debt settlement company will contact the creditor and negotiate a lump-sum payoff of the debt, ideally at a highly reduced percentage. The consumer then uses the money that he/she has been saving to pay the lump-sum, and can then have the benefit of a significant portion of their original debt being forgiven.

5. Because of its theoretical potential for a quick turnaround and significant savings, debt settlement is often promoted emphasizing these facts. For example, Defendant FH Financial prominently represents on its web site that consumers will "Save 40-60%" with a payoff in 36 months. Debt settlement companies may also disparage the alternative forms of debt relief in order to persuade consumers that settlement is the best option for them. For example, Defendant FH Financial advises potential customers that, "Bankruptcy should be considered as only an absolute last option," and that in bankruptcy, "You will most likely lose your large assets such as cars, home, investment accounts." In reality, the debt settlement company has no interest or ability to advise consumers on the best option for them, rather they are selling their program.

6. Because debt settlement only works if consumers are not making monthly payments on their unsecured debts (since creditors will not want to settle a debt if they are receiving monthly payments), there are inherent risks involved with participating in a debt settlement program, that can have catastrophic effects to the consumer. Specifically, consumers entering a debt settlement program may experience any, or all, of the following:

- A. Creditors will continue to assess interest, late fees, over-limit charges, and any other fees associated with the account. As a result, at the time that a settlement is reached, the consumer owes significantly more on their account, thus reducing the actual savings.
- B. Creditors are under no obligation to accept, or even entertain, a settlement offer. When this occurs, consumers are stuck with a vastly higher balance because of the interest and late fees that have accumulated on the debt. As a result, the consumer can end up in a far worse financial situation than when they entered the program.
- C. Because they are no longer receiving monthly payments, creditors will likely engage in collection activities which may include repeated phone calls and other correspondence. Over time, these activities can increase, especially as the consumer's account may get transferred to a collection agency.
- D. Once a consumer stops paying on their accounts, the creditor may file a lawsuit against the consumer for breaking their contract. Most debt settlement companies, including Defendant, cannot offer any assistance when a lawsuit is filed, and as a result the consumer can end up with multiple judgments against them.
- E. The consumer's credit reports will reflect the late charges and nonpayment of their unsecured debt. As a result, the consumer's credit score will drop while participating in the program, and the consumer may experience the long term effects of a low credit score, which can include difficulty in buying a house or car, obtaining insurance, or obtaining employment.
- F. The debt forgiveness that occurs as part of the settlement is taxable income.

7. Because debt settlement is generally a "for-profit" industry, companies charge their customers large fees. Fees are typically calculated as a percentage of the total debt the consumer brings into the program, are often collected in the first several months of the program, and are for the most part non-refundable. In addition, there may be monthly maintenance fees, enrollment fees, administrative fees, and back-end settlement fees. As a result, the high fees cut into the potential savings that a consumer can experience in the program. Moreover, these fees may be the tip of the iceberg for consumers - if they are sued and want an attorney they may have to pay a lawyer's legal fees, if they want to improve their credit after participating in the settlement program they may have

to pay a credit repair firm's fees, and if they want tax advice regarding debt forgiveness, they may need to pay an accountant.

8. Because of the additional costs and negative effects of debt settlement, it is often difficult to say what a consumer's true cost is in a program, or what benefit they may really see. For example, a consumer with a \$10,000 unsecured debt may be told their debt can settle for \$4,000, or a 60% savings, but when the company's fees are added, along with whatever costs are associated with improving the damage caused by the settlement process, the consumer likely will spend far more than \$4,000 in resolving the debt. In addition, late fees and interest will likely increase the \$10,000 debt, such that a 60% settlement will actually be for much more than \$4,000. Add to this the risk that a creditor will not settle an account, and it becomes evident that debt settlement is a risky form of debt management, that requires clear disclosures to consumers so that they can make an informed decision.

DEFENDANT

9. Defendant FH1 Financial Services, Inc. is a Texas for-profit corporation formed in February of 2006. Defendant FH1 Financial Services, Inc. does business under the assumed name "FH Financial Service." FH Financial has two directors, Jacob Hunt, who also serves as President of the corporation, and Alexander Fender, who also services as vice president of the corporation. Defendant FH1 Financial Services, Inc. can be served with process through its registered agent, Alexander T. Fender, Jr., 4230 LBJ Freeway, Suite 125, Dallas, Texas 75244.

VENUE

10. Venue of this suit lies in Travis County, Texas pursuant to the DTPA §17.47(b), because Defendant has done business in Travis County, Texas.

PUBLIC INTEREST

11. Because Plaintiff STATE OF TEXAS has reason to believe that Defendant has engaged in and will continue to engage in the unlawful practices set forth below, Plaintiff STATE OF TEXAS has reason to believe that Defendant has caused and will cause adverse effects to legitimate business enterprise which conducts its trade and commerce in a lawful manner in this State. Therefore, the Consumer Protection and Public Health Division of the Office of the Attorney General of Texas believes and is of the opinion that these proceedings are in the public interest and at least seven days prior to instituting this action contacted Defendant to inform it in general of the alleged unlawful conduct.

TRADE AND COMMERCE

12. Defendant is engaged in trade and commerce as that term is defined by § 17.45(6) of the DTPA.

ACTS OF AGENTS

13. Whenever in this Petition it is alleged that Defendant did any act, it is meant that:
- A. Defendant performed or participated in the act; or
 - B. Defendant's officers, agents, or employees performed or participated in the act on behalf of and under the authority of the Defendant.

STATEMENT OF FACTS

14. Defendant FH Financial operates a web site at www.fhfinancialservice.com, on which it advertises its debt settlement program, which is available nationwide including in Travis County, Texas. Although Defendant represents that it can provide numerous options of debt relief to consumers, including debt management, consumer credit counseling and debt settlement, in reality

Defendant only sells a debt settlement program. Defendant's web site includes several representations regarding the benefits of its program:

- A. "FH Financial will eliminate your debt."
- B. "DEBT FREE in 18 to 36 Months!"
- C. "The Most Effective Consumer Debt Reduction Program in the Nation"
- D. "Save 40-60%"
- E. "Better Credit Score"
- F. "FH Financial is the only company that has working relationships with all creditors to negotiate your debt and establish a one time cash settlement or a settlement with a payment plan."
- G. "FH Financial Debt Settlement Plan has a 99.3% success rate"

15. On its web site, Defendant further describes alternative forms of debt relief. For example:

- A. "Bankruptcy is a complex process and does not provide immediate relief; you will be under constant stress and you will live with it on your record for the rest of your life. Although it will remain on your credit report for 7-10 years, every loan application and most employment applications ask 'have you ever filed for bankruptcy?' Bankruptcy will follow you for the rest of your life."
- B. Further representations regarding bankruptcy include: "You will probably lose your large assets such as cars, home, investment accounts," "You most likely will payback more through bankruptcy compared to a Debt Settlement Plan," "Bankruptcy is a public record filing within the judicial system; bankruptcy will stay with you to the grave," and "You will pay the legal costs associated with bankruptcy, court fees, and the repayment plan the trustee assigns".
- C. The following is represented regarding credit counseling: "Not all debts qualify," "Your payment is not significantly lower than your current minimums," "Most people do not resolve their debt with credit counseling," "You will payback the full amount that you owe plus interest plus monthly fees," "No guarantee that you will be out of debt in the time frame of the plan," "No guarantee that your interest rates will stay low," and "Long term negative impact on credit score."

- D. Defendant compares its debt settlement services to those alternative forms of debt relief - but the only "cons" described for debt settlement are that it "[m]ay negatively affect your credit if you haven't fallen behind yet;" "[y]our creditors do not get paid monthly;" and "[y]ou will not be able to attain a loan during the course of the plan" *Sic*. In comparing its services to bankruptcy, Defendant states: "...bankruptcy attorneys have little information on other debt relief options. . . [i]f you want a comprehensive review, you may receive one free and under no obligation from a Debt Counselor at FH Financial;" and in comparing the costs of bankruptcy and debt settlement, Defendant represents that "Debt settlement will cost you 30% less."

16. Consumers interested in enrolling in Defendant's program can call FH Financial via a toll-free number provided on the web site. During the sales call, Defendant continues the representations made on the web site, including:

- A. It will take three years or less to complete the program.
- B. As soon as the consumer pays the required amount into the program, they will be debt free.
- C. Creditors are now taking as little as 10 cents on the dollar because they are hurting for money.
- D. While the consumer's credit score will temporarily go down by 50 to 100 points, the consumer's credit score will improve during the term of the debt settlement plan, and will be higher at the plan's conclusion than it ever was, even qualifying them for a zero interest auto loan.
- E. FH Financial has a good record with the Better Business Bureau, with "only" five complaints on file.

17. In reality however, the representations and promises made by FH Financial as described above are often false, or at best misleading, and contain several material omissions regarding Defendant's, or any, debt settlement program. These include:

- A. FH Financial cannot know at what percentage consumers' debts will settle for, nor can they know how long it will take to complete Defendant's program. Indeed, since nothing requires creditors to settle at a particular rate, or even accept a settlement, FH Financial cannot know what individuals' experiences will be - especially since it does not know who the consumers' creditors are at the time of the representations.

- B. FH Financial's program, like all debt settlement programs, can often result in long-term negative effects on the consumer's credit.
- C. FH Financial's description of credit counseling and bankruptcy is inaccurate, and FH Financial is not a law firm qualified to provide legal advice regarding bankruptcy.
- D. FH Financial has an "F" rating with the BBB - information it specifically redacts when it sends consumers its BBB report.
- E. FH Financial has no special or unique relationships with creditors.

18. FH Financial fails to disclose the negative effects of its, or any, debt settlement program. These include increased collection efforts, the risk of lawsuits, the fact that creditors may not accept any settlement, the fact that debt forgiveness is taxed as income, the fact that late fees and interest will increase the amount of the consumer's debt, the fact that Defendant cannot work with certain creditors, and the negative effects on the consumer's credit. Indeed, Defendant further perpetuates this misrepresentation by disparaging other forms of debt relief, such as credit counseling, even though almost every negative representation about credit counseling is also true regarding debt settlement. By omitting this material information, and disparaging other forms of debt relief, Defendant misleads consumers into believing that FH Financial's debt settlement program is the only viable option, no matter what the consumers unique situations may be.

VIOLATIONS OF DTPA

19. Plaintiff, the State of Texas, incorporates and adopts by reference the allegations contained in each and every preceding paragraph of this petition.

20. Defendant, as alleged and detailed above, has in the course of trade and commerce engaged in false, misleading and deceptive acts and practices declared unlawful in § 17.46(a) and (b) of the DTPA. Such acts include:

- A. Engaging in false, misleading or deceptive acts or practices in violation of § 17.46(a) of the DTPA.
- B. Representing that goods or services have sponsorship, approval, characteristics, ingredients, uses, benefits, or quantities which they do not have or that a person has a sponsorship, approval, status, affiliation, or connection which he does not in violation of § 17.46(b)(5) of the DTPA.
- C. Disparaging the goods, services, or business of another by false or misleading representation of facts in violation of § 17.46(b)(8) of the DTPA.
- D. Advertising goods or services with intent not to sell them as advertised in violation of § 17.46(b)(9) of the DTPA.
- E. Representing that an agreement confers or involves rights, remedies, or obligations which it does not have or involve, or which are prohibited by law in violation of § 17.46(b)(12) of the DTPA. And,
- F. Failing to disclose information concerning goods or services which was known at the time of the transaction if such failure to disclose such information was intended to induce the consumer into a transaction which the consumer would not have entered into had the information been disclosed in violation of § 17.46(b)(24) of the DTPA.

PRAYER

21. By reason of the acts and practices described herein above, DEFENDANT has violated and will continue to violate the laws as herein alleged unless enjoined by this Honorable Court.

22. WHEREFORE, PREMISES CONSIDERED, Plaintiff prays that DEFENDANT be cited according to law to appear and answer herein; that after due notice and hearing a temporary injunction be issued; and that upon final hearing a permanent injunction be issued, restraining and enjoining DEFENDANT, its officers, agents, servants, employees and attorneys and any other person in active concert or participation with DEFENDANT, from engaging in the following acts or practices:

- A. Representing to consumers that Defendant will settle consumers' debts for a certain percentage of the debt, or within a certain percentage range, unless Defendant has a substantial basis in fact for the representations. For purposes of compliance with this term, the substantial basis in fact shall be:
 - (i) Contractual agreements with creditors to settle debts with clients of the Defendant at the represented percentage of the debt, or within the represented percentage range, or
 - (ii) A documented record of at least three years of settlement data which reflects that at least 75% of accounts handled by Defendant settled at or below the represented percentage or percentage range.
- B. Failing to inform consumers that Defendant cannot assist with certain types of debt, including but not limited to, student loans.
- C. Failing to disclose that consumers may be sued by their creditors if they are enrolled in Defendant's program.
- D. Failing to disclose to consumers that Defendant will not be able to assist the consumer with any lawsuit that is filed by a creditor against the consumer.
- E. Failing to disclose to consumers that enrollment in Defendant's program will likely result in increased collection efforts by the consumers' creditors.
- F. Misrepresenting Defendant's ability to cease contact and collection efforts by the consumers' creditors.
- G. Misrepresenting Defendant's ability to settle with all creditors, or at any particular rate with those creditors.
- H. Failing to disclose to consumers any creditors who refuse to work with Defendant and/or any other debt settlement companies.
- I. Failing to disclose that a consumer's debt will continue to increase while the consumer is participating in Defendant's debt settlement program, including but not limited to:
 - (i) Increases due to compounding interest;
 - (ii) Late fees and other penalties for nonpayment; and
 - (iii) Increased interest rates due to default.

- J. Failing to disclose to consumers that the amount of debt they are ultimately required to pay in order to resolve a debt obligation may be far larger than the amount of debt with which they enter Defendant's program.
- K. Failing to disclose that Defendant cannot guarantee that the consumers' creditors will agree to settle with the consumers for any amount less than the full amount owed.
- L. Failing to disclose that consumers will owe taxes on forgiven debt amounts.
- M. Making any false or misleading representations regarding bankruptcy, credit counseling, or other forms of debt relief.
- N. Misrepresenting Defendant's ability to provide tax, legal, accounting, or credit repair advice.
- O. Misrepresenting Defendant's experience or past success in debt settlement.
- P. Misrepresenting the effects of debt settlement, or any other form of debt relief, on a consumer's credit score.

23. Plaintiff further requests that upon final hearing this Court award such relief as the Court finds necessary to redress injury to consumers including, but not limited to, restitution of monies paid by consumers; and further order Defendant to pay to the State of Texas:

- A. Restitution of monies paid by consumers.
- B. Disgorgement of any ill-gotten gains.
- C. Civil penalties of up to \$20,000.00 per violation of the DTPA.
- D. Pre-judgment and post-judgment interest on all awards of restitution, damages, or civil penalties, as provided by law. And,
- E. All costs of Court, costs of investigation, and reasonable attorneys fees pursuant to TEX. GOVT. CODE ANN. § 402.006(c).

24. Plaintiff further prays for such other relief to which Plaintiff may be justly entitled.

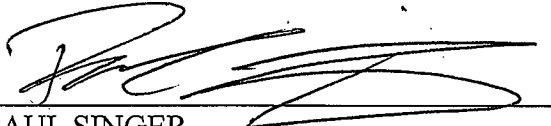
Respectfully submitted,

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First Assistant Attorney General

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PAUL D. CARMONA
Chief, Consumer Protection and Public Health Division

A handwritten signature in black ink, appearing to read 'Paul Singer', written over a horizontal line.

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